No. 14,879

United States Court of Appeals

For the Ninth Circuit

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, as Executor of the Last Will and Testament of Thomas McDonough, deceased,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLANT'S OPENING BRIEF.

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JURISDICTIONAL STATEMENT.

This is an appeal from a judgment of the District Court of the United States for the Northern District of California, Southern Division. The opinion of the Court below is reported at 130 Fed. Supp. 923 and is set forth in the record herein (R 71). Appellant is a national banking association organized and existing under and by virtue of the laws of the United States of America. Its principal place of business is in the City and County of San Francisco, State of California, and in the Northern District of California,

Southern Division. It is the duly appointed and qualified executor of the Last Will and Testament of Thomas McDonough, who died in San Francisco, California, on September 13, 1948, leaving a Last Will and Testament wherein plaintiff was named executor thereof (R 3 and 4, paragraphs 2 and 3, admitted in answer, R 19, paragraphs 2 and 3).

The action arises under the Internal Revenue laws of the United States and is for the recovery of estate taxes assessed against and collected from the appellant with respect to the estate of said Thomas McDonough by the appellee through its agents, James G. Smythe and Charles F. Masarik, Jr., the then Collectors of Internal Revenue for the First District of California, neither of whom was in office as Collector of Internal Revenue at the time this action was commenced (R 3, 4 and 5, paragraphs 1, 4, 5, 6, admitted in answer, R 19, paragraphs 1, 4, 5 and 6). After the payment of said taxes the appellant duly filed written claim for refund thereof as provided by law and said claim was rejected by the appellee through its agent, the Commissioner of Internal Revenue, on March 3, 1953 (R 5, paragraph 7, admitted in answer, R 20, paragraph 7).

This action was commenced in the District Court on May 8, 1953 (R 19). It was brought pursuant to the provisions of Section 1346 of the Judicial Code, USC Title 28, and arises under the Internal Revenue Code of February 10, 1939, C. 2, 53 Stat. 1, as amended, Sections 800 to 937 (Sections 800 to 937, Chapter 3, Estate Tax of Subtitle A, Title 26 USCA)

(R 3, paragraph 1, admitted by answer, R 19, paragraph 1).

The matter came on for trial before the District Court and the judgment of that Court was entered June 20, 1955 (R 80). On August 15, 1955, under Sections 1291 and 1294 of the Judicial Code, USC Title 28, appeal was taken to this Court to review the judgment of the Court below (R 80). This appeal and transcript of record were filed and docketed in this Court on September 21, 1955 (R 106).

STATEMENT OF THE CASE.

(a) Nature of the Case.

This case involves the Federal estate tax liability of the estate of Thomas McDonough, who died September 13, 1948. At the time of his death he owned property which he had acquired as surviving joint tenant from Peter P. McDonough, who died July 8, 1947, and which property had been included as part of the gross estate in the estate tax return filed for the estate of Peter P. McDonough. At times Peter P. McDonough will be referred to herein as the first decedent and Thomas McDonough as the present decedent.

The Federal estate tax is a tax at certain rates upon the net estate of the decedent. The net estate is the gross estate less certain deductions and exemptions. The gross estate includes all of the property of the decedent. (Section 811 of the Internal Revenue Code of 1939.) The deductions (Section 812 of the

Internal Revenue Code) include a deduction for property previously taxed which is described as an amount equal to the value of any property (1) forming a part of the gross estate situated in the United States of any person who died within five years prior to the death of the decedent where such property can be identified as having been received by the decedent from such prior decedent by gift, bequest, devise or inheritance. It is further provided that this deduction shall be allowed only where an estate tax was finally determined and paid by or on behalf of the estate of such prior decedent, and only in the amount finally determined as the value of such property in determining the value of the gross estate of such prior decedent, and only to the extent that the value of such property is included in the decedent's gross estate. (Section 812(c) of the Internal Revenue Code of 1939.)

In this case it is stipulated that the present decedent owned at the time of his death property acquired from the first decedent of a value of $585,719.23 and that such property when included in the estate of the first decedent was included therein at a value of $577,971.92 (R 23 and 24, paragraph 4(b) and paragraph 5).

Most of the net estate of the first decedent was made up of the property acquired by the present decedent. The estate tax of the first decedent had not been settled and paid until after the present decedent had died, and the amount of that tax paid by the present decedent's estate was $141,592.71, all attrib-

utable to said jointly owned property (R 23 and 24, paragraphs 4(e) and 4(f)).

The statutory provision authorizing the deduction for property previously taxed (Section 812(c)) first provides for the amount at which such deduction should be identified and valued. It then provides for the application of certain mathematical computations to reduce the first value by certain adjustments. No issue is raised in this appeal as to the calculation of these adjustments, but they will have to be recalculated should this Court reverse or modify the decision of the Court below. The sole issue relates to the initial evaluation for the deduction before adjustment through the mathematical computations, and as to this issue the appellant contends that the property previously taxed should be identified and evaluated at the amount of $577,971.92 at which it was included in the gross estate of the first decedent. The Government contends it should be valued at the gross value less the Federal estate taxes and other charges against the first decedent's estate.

The District Court decided in favor of the Government.

(b) Facts.

The facts are not in dispute. They are set forth in the complaint (R 3-12) as admitted by the Answer (R 19-21), and in the Pre-Trial Order (R 21-24), as follows:

Peter P. McDonough died in San Francisco, California, on July 8, 1947. At the time of his death he

and his brother, Thomas McDonough, owned certain property as joint tenants. One half of the value of this property, or $577,971.92 (R 23) was included in Peter's gross estate for purposes of determining his Federal estate tax liability, which amounted to $149,289.84. The part of this Federal estate tax which was attributable to the joint tenancy property was $141,592.71 (R 24).[1]

The said joint tenancy property passed to Thomas before the tax owed by Peter's estate was paid, and the tax remained unpaid at the death of Thomas on September 13, 1948. Subsequently, it was paid, $141,686.05 by Thomas' executors on October 8, 1948.

The said joint tenancy property was owned by Thomas at the time of his death, and the gross value of said property included and identified in the Estate of Thomas as having been received by him from Peter, without taking account of any proportionate amount of the Federal estate tax in Peter's estate, was the sum of $585,719.23 (R 24).

On the Federal estate tax return filed for the Estate of Thomas, the deduction for property previously taxed was computed by identifying the property acquired from Peter at its gross value less Peter's Federal estate tax of $141,686.05 attributable thereto (R 78). Appellant contends in this action that the return was in error in reducing the gross value by the tax for the purpose of determining the deduction in Thomas' estate for property previously taxed.

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[1]Originally computed at $141,686.05 but finally determined in later Government audit to be $141,592.71.

In the Government's audit of the estate tax return for Thomas' estate, the identifying value of the property previously taxed was computed as follows (R 65):

Total gross estate of Peter		$638,673.66
Less deductions claimed and allowed		27,093.53
Net		$611,580.13
Less:		
Federal estate taxes	$149,289.84	
Inheritance taxes	49,263.81	
Net specific legacies to others than Thomas	39,116.47	207,670.12
Theoretical balance of property previously taxed in present (Thomas) estate		$373,910.01
Adjustment		15.23
Identified property previously taxed		$373,894.78

This amount was then used as the basis for the mathematical computations for proportionate reductions (R 63-64). Appellant contends that there is no statutory basis for the method used by the Government in identifying the "theoretical" value of property previously taxed.

The District Court sustained the Government both in the finding that $373,894.78 represented the net value of the interest of Thomas in the property previously taxed in Peter's estate (R 76-77), and in the legal conclusion that for the purpose of the property previously taxed deduction in Thomas' estate, the property is to be identified only at its net value after deducting from its gross value the amount of the Fed-

eral estate taxes attributable thereto and other debts and charges in Peter's estate (R 78). In its Statement of Points on Appeal, appellant sets forth these findings and conclusions as alleged errors, both as findings of fact not supported by the evidence, and conclusions of law not in accord with the controlling statutory provisions (R 107-110).

None of the items making up the $207,670.12 of reductions shown in the Government's computation above tabulated are deductions for estate tax purposes and none were deducted in the estate of Peter McDonough in determining the estate tax liability of that estate, but credit was allowed for inheritance taxes.

(c) Issues Involved.

(1) Is the Government's determination of the "identified property previously taxed" as $373,894.78 (R 65) correct in the light of the agreed fact that property included in the first decedent's gross estate at a value of $577,971.92 was identified as owned by the present decedent at the time of his death and had a value at that time of $585,719.23.

(2) In determining the identified value of such previously taxed property, is it proper to reduce the value of such property by Federal estate taxes against the first decedent's estate unpaid at the time of death of the present decedent?

(3) Where property included in the gross estate of a decedent is identified as having been included in the gross estate of a prior decedent, does the provision of Section 812(c), Internal Revenue Code of 1939,

to the effect that the property previously taxed shall be determined "in the amount finally determined as the value of such property in determining the gross estate of such prior decedent, and only to the extent that the value of such property is included in the decedent's gross estate * * *" mean the *gross estate* valuation of such property or the gross estate valuation less the Federal estate tax liability of the prior decedent's estate unpaid at time of the present decedent's death?

STATUTES INVOLVED.

Chapter 3 of the Internal Revenue Code of 1939. The pertinent text of Sections 810, 811, 812 and 827 particularly applicable is set forth in Appendix A attached.

SPECIFICATION OF ERRORS RELIED UPON.

The specification of errors relied upon is set forth in Appellant's Statement of the Points on which it intends to rely (R 107-110), as follows:

(1) The judgment and decision is against law.

(2) The Findings of Fact do not support either the Conclusions of Law or the Judgment.

(3) That portion of Finding 4 reading as follows is not supported by the evidence, and in fact is a conclusion of law, and said conclusion of law is erroneous, to wit:

"The net value of said jointly-owned property to which Thomas McDonough succeeded by virtue of the death of Peter P. McDonough was $373,910.01, computed by deducting from the gross estate of Peter P. McDonough the specific legacies, the federal estate taxes, the state inheritance taxes and the deductions in the amounts set forth above."

(4) That portion of Finding 5 reading as follows is not supported by the evidence, and in fact is a conclusion of law, and said conclusion of law is erroneous, to wit:

"This left a net adjusted value of the interest of Thomas McDonough in the jointly-owned property included in the prior estate and included in Thomas McDonough's estate to which interest Thomas McDonough succeeded on Peter P. McDonough's death of $373,894.78."

(5) Failure to find that the amount of property previously taxed within five years received by Thomas McDonough from Peter P. McDonough, which was entitled to be deducted from the gross estate for Federal estate tax purposes in the Estate of Thomas McDonough, was the sum of $577,971.92.

(6) Failure to find that in computing the Federal estate tax due from the Estate of Thomas McDonough, said estate was entitled either to have the full amount of said jointly-owned property included in the gross estate of said Thomas McDonough with a credit for the amount of the Federal estate tax of $141,592.71 due and unpaid in the Estate of Peter P. McDonough, with a deduction of said previously taxed property

amounting to $577,971.92; or, in the alternative, to have the gross estate of Thomas McDonough reduced by the said tax of $141,592.71, and still be entitled to a deduction of $577,971.92 for the property previously taxed in the Estate of Peter P. McDonough.

(7) Failure to find that notwithstanding the form in which the gross estate for Federal estate tax purposes was set forth in the estate tax return in the Estate of Thomas McDonough, plaintiff nevertheless was entitled in computing the deduction for property previously taxed in the Estate of Peter P. McDonough to have such computation made in accordance with the Federal estate tax provisions, i.e., the applicable law, at the full amount of $577,971.92.

(8) That said judgment is against law in that it did not compute the jointly-owned property previously taxed in the Estate of Peter P. McDonough at the full value of $577,971.92.

(9) That said judgment is against law in that it holds that the Federal estate tax of $141,592.71 paid by the Estate of Thomas McDonough upon the joint property left by Peter P. McDonough and due in said Estate of Peter P. McDonough, had to be deducted from said jointly-owned property of $577,971.92 in computing the deduction in the Estate of Thomas McDonough for property previously taxed.

(10) That said judgment is against law in that it reduced the deduction for property previously taxed in the Estate of Peter P. McDonough by the items set forth in Finding 4.

SUMMARY OF ARGUMENT.

Section 812(c) describes exactly how the property previously taxed deduction should be computed. The theoretical computations applied by the Government in determining what it calls "theoretical balance of property previously taxed in present estate" have no support from any provision of Section 812(c).

The property previously acquired from Peter McDonough and owned by Thomas McDonough at time of his death, must be included in Thomas' gross estate at its fair market value. Therefore, under the provision in Section 812(c) that the property previously taxed shall be "in the amount finally determined as the value of such property in determining the gross estate of such prior decedent and only to the extent that the value of such property is included in the decedent's gross estate", the identifiable value of the property previously taxed is the fair market value (gross estate value) of the jointly owned property. The Government and the Court below erred in concluding that the "value" referred to in the above quoted provision of Section 812(c) is the gross estate value reduced by the deduction for the unpaid Federal estate taxes of Peter's estate.

Since the identified property was included in the gross estate of Peter at a value of $577,971.92, and since its fair market value at which it is includible in the gross estate of Thomas is $585,719.23, the lesser of these two amounts, or $577,971.92, is the identifiable value of the property for the purpose of computing the property previously taxed deduction under Section 812(c).

ARGUMENT.

This is a case where a technical statute prescribes exactly what must be done to comply with it. Difficulty and confusion has arisen because of the inclination of some of the Courts who have considered similar matters, to digress from the literal wording of the statutes to accomplish what seemed to them to be the fair result. In doing this the Courts have invaded the field of legislation, and have made it difficult to either reconcile different views, or to determine an exact rule of statutory construction, with respect to their application of this statute (Section 812(c)) regarding the deduction for property previously taxed.

Turning to an analysis of the statute—Section 812(c)—and its applicability to this case, it provides that property previously taxed shall be

> (1) "An amount equal to the value of any property (1) forming a part of the gross estate situated in the United States of any person who died within five years prior to the death of the decedent * * * where such property can be identified as having been received by the decedent * * * from such prior decedent by gift, bequest, devise or inheritance * * *."

It is acknowledged in this case that the present decedent died September 13, 1948, that the first decedent died July 8, 1947, that the present decedent owns property identified as acquired from the prior decedent by inheritance (it being recognized that the word "inheritance" includes transfers under right of survivorship (*Commissioner v. Fletcher Savings &*

Trust Co., Exec. (1932), 59 F. (2d) 508, affirming 20 BTA 1049), and that it formed a part of the gross estate of the prior decedent at a value of $577,971.92 (R 23-24).

(2) The Section then provides—

> "This deduction shall be allowed only where * * * an estate tax imposed under this chapter * * * was finally determined and paid by or on behalf of * * * the estate of such prior decedent * * * and only in the amount finally determined as the value of such property in determining the * * * gross estate of such prior decedent, and only to the extent that the value of such property is included in the decedent's gross estate * * *."

It is acknowledged in this case that an estate tax was finally determined against the first decedent's estate attributable to this property and was paid by the executor of the present decedent's estate; further, that the value of such property was $577,971.92 *in determining the gross estate of the prior decedent,* and was $585,719.23 *in determining the gross estate of the present decedent without taking into account the Federal estate tax against the first decedent's estate.*

(3) The Section then provides that—

> "Where a deduction was allowed of any mortgage or other lien in determining the * * * estate tax of the prior decedent, which was paid in whole or in part prior to the decedent's death, then the deduction allowable under this subsection shall be reduced by the amount as paid."

In this case the "lien" is the Federal estate tax on the prior decedent's estate; such lien was *not* allowed as a deduction in determining the estate tax of the prior decedent; such "lien" was not paid prior to the present decedent's death but was paid by his estate; so this provision is inapplicable to this case.

(4) The Section then provides for several mathematical computations for reductions of the property previously taxed evaluation. The computations and reductions made in this case will have to be recalculated should the Court reverse or modify the decision of the lower Court (R 24 para. 6).

It seems indisputable that under the provisions of Section 812(c) above analyzed, when applied to this case, the "value" of the property previously taxed is $577.971.92, and there is no justification whatever for the Government's action in reducing it by the Federal estate taxes paid on the first decedent's estate, and in concluding in effect that the gross evaluation of property previously taxed should be the present decedent's "equity" in the property rather than the value at which such property was included "in determining the gross estate of the prior decedent".

The District Court, in its opinion, observed that decided cases "express conflicting views as to the correct method of valuing the deduction", (R 73) and then concluded "it would seem that the value of property received from a decedent could never be greater than the value of his property less all of the taxes, legacies, claims and charges outstanding against it * * * the value of such property received by an heir

is only the net value after all the claims against the property have been subtracted" (R 73-74). The Court made no detailed analysis of Section 812(c) in its written opinion in arriving at this conclusion.

As hereinabove pointed out the Section is specific in requiring that "this deduction shall be allowed * * * in the amount finally determined as the value of such property in determining * * * *the gross estate* of such prior decedent, and only to the extent that the value of such property is included in the decedent's *gross estate* * * *" (italics ours). It is admitted that the value of such property in determining the *gross estate* of the prior decedent was $577,971.92 (R 23). It is admitted that the *"gross value"* of such property identified in the present decedent's estate is $585,719.23 (R 24) without taking into account the $141,592.71 proportionate amount of the Federal estate tax against the prior decedent's estate. If the $585,-719.23 is the value at which such property must be included in the present decedent's *gross estate* it is obvious that under the above quoted provision of Section 812(c) the identifiable valuation of such property previously taxed is $577,971.92 since it is the lesser amount.

The only possible support for the contention that the $577,971.92 value is not the value of the previously taxed property under Section 812(c) must be that for some reason the tax indebtedness of $141,592.71 must be applied against the property value of $585,719.23 in determining how much of that value should be included in the *gross estate* of the present decedent. Reducing the matter to simple words—in the deter-

mination of the present decedent's *gross estate,* is the tax obligation something that must be applied against the fair market value of the present decedent's property before determining how much of that value is includible in the *gross estate;* or, is the tax obligation a deduction which does not affect the gross estate but is to be used merely in the "deduction" category in arriving at the net taxable estate.

It would seem that the very structure of the estate tax statute and the specific provision of Section 812(b) should answer that argument. Section 812(b) lists as *deductions* (1) funeral expenses (2) administration expenses (3) claims against the estate, and, most important to this particular case, (4) unpaid mortgages upon, or any indebtedness in respect to, property where the value of the decedent's interest therein, undiminished by such mortgage or indebtedness, is included in the value of the gross estate. It is also significant that Section 812(c) itself speaks of a situation "where a deduction was allowed of any mortgage or other lien in determining the * * * estate tax * * *", indicating that mortgages, liens or other charges against the property are reportable as deductions and do not change the requirement that the gross value of the property must be reported in the gross estate.

In Treasury Department Regulation 105, Section 81.38, it is provided:

> "Deduction is allowed of the full unpaid amount of a mortgage upon, or of an indebtedness in respect of, any property of the gross estate * * * provided the value of the property,

undiminished by the amount of the mortgage or indebtedness, is returned as part of the value of the gross estate. If decedent's estate is liable for the amount of the mortgage or indebtedness, the full value of the property subject to the mortgage or indebtedness *must* be included as part of the value of the gross estate; the amount of the mortgage or indebtedness being in such case allowed as a deduction. But if the decedent's estate is not so liable, only the value of the equity of redemption (or value of the property less the indebtedness) need be returned as part of the value of the gross estate."

Section 827 of the Internal Revenue Code, provides as follows:

"(a) *Upon Gross Estate.*—Unless the tax is sooner paid in full, it shall be a lien for ten years upon the gross estate of the decedent, except that such part of the gross estate as is used for the payment of charges against the estate and expenses of its administration, allowed by any court having jurisdiction thereof, shall be divested of such lien. * * *

"(b) *Liability of Transferee, Etc.*—If the tax herein imposed is not paid when due, then the spouse, transferee, trustee, surviving tenant, * * * who receives, or has on the date of the decedent's death, property included in the gross estate under section 811(b), (c), (d), (e), (f), or (g), to the extent of the value, at the time of the decedent's death, of such property shall be personally liable for such tax. * * *"

Since under Section 827 supra, Thomas McDonough, and his estate were *personally* liable for the Federal

estate taxes on Peter McDonough's estate to the extent of the value of the jointly held property included in Peter's estate, upon which property such obligation was a lien, it follows that under the Regulation Sec. 81.38 above quoted, the full value of the property or $587,719.23 *must* be included in Thomas' gross estate and the indebtedness for the taxes *must* be shown as a deduction. The identifiable value, therefore, of the property previously taxed to be used in computing the property previously taxed deduction in the estate of Thomas would be the $577,971.92 value used "in determining * * * the gross estate of" Peter since such value is less than the $585,719.23 value at which such property is includible in the gross estate of Thomas.

The conflicting pertinent Court decisions are not too helpful primarily because they fail to analyze all the provisions of Section 812(c) and the manner in which the mathematical adjustment calculations required in the latter part of the Section rectify any tendency to unfair results from strict application of the first few paragraphs of the Section.

In the case of *Bahr v. Commissioner,* CA-5 (1941), 119 F. (2d) 371, involving much the same question as is involved in this case the Court touched upon the nature of the first decedent's estate tax liability as follows:

> "For present purposes Frank's fourth of the debts were an incumbrance on Frank's property and not 'claims against the estate' of Eugene. The two things are clearly distinguished in the tax statute and regulations; Sect. 303(a)(1), as amended by Revenue Act 1932, § 805, 26 U.S.C.A.

Int. Rev. Acts, page 232; Reg. 80, Art. 38. That section, providing for deductions, after naming funeral and administration expenses, mentions: (C) Claims against the estate, and (D) Unpaid mortgages upon or any indebtedness in respect to property, where the value of decedent's interest therein, undiminished by such mortgage or indebtedness, is included in the value of the gross estate. Frank's part of the debts, a lien on his part of the property, is 'such mortgage or indebtedness.' Subsection D permits, so far as it is concerned, either that the net value of the property be put in the gross estate in which case the indebtedness may not be deducted, or else the full value may be included in the gross with a contra deduction. There is, as the Board remarks, no difference thus far which is done.

"But when we come to Sec. 303(a)(2), as amended by Sect. 806(a) of the Revenue Act of 1932, which deals with the deduction of property which has caused estate taxes within five years preceding, it does make a difference, both in the basis of this deduction, and in the subtraction from it of the result of the formula with which subparagraph (a)(2) ends. The purpose of these provisions is to avoid a double estate or gift tax on the same property within five years."

The Court then decided that the identified property should be reported in the second decedent's estate as though the taxes had been paid out of that property before the death of the second decedent, and concluded:

"The Federal estate tax and State inheritance tax assessed against the Estate of Frank, though

> paid by petitioners after the death of Eugene, are not claims against the estate of Eugene. They go to reduce the value of property received by Eugene's estate from Frank's, along with his fourth of the partnership debts and administration charges, as the Commissioner ruled. The decision of the Board of Tax Appeals is affirmed".

Judge Hutcheson dissented on the ground that the statute required that the property be valued at its gross value and should not be reduced by the charges and Federal estate tax liabilities of the earlier estate, saying,

> "It will not do then for the Board to say to the petitioners we think the method employed by us is more nearly right and just than the one you invoked. For this is not to apply but to rewrite the section. It must be able to point out that its determination is in accordance with the section as amended and not as it formerly was. It has failed to do this."

Six years later, in the case of *Thomas v. Earnest,* CA-5 (1947), 161 F. (2d) 845, this same Court adopted Judge Hutcheson's dissent in the *Bahr* case, to the extent of deciding that the gross value of the property should *not* be reduced by the Federal estate tax liability of the first decedent's estate. The *Bahr* case, as modified by the *Thomas* case, supports appellant's position here.

In the case of *Central Hanover Bank and Trust Company v. Commissioner,* CA-2 (1947), 159 F. (2d) 167, a somewhat similar question was involved though somewhat distinguishable because the Federal estate tax on the first decedent's estate was paid by the sec-

ond decedent prior to his death. The Court, after admitting that there were conflicting views on the subject, concluded that under Section 812(c) the "identification" of the property previously taxed meant not the physical identity of the assets but rather the identity of the legatee's net financial interest in it. In a similar case the Court of Claims reached the same conclusion in the case of *Bloedorn v. The United States* (1953), 116 Fed. Supp. 133, this Court too recognizing that there were conflicting views, and Judge Littleton dissenting. (To same effect *McCarthy v. Delaney,* Dist. Ct. Mass. (1948), 76 F. Supp. 471, and *Est. of Roswell Ackley,* 23 TC No. 84.)

No reference was made in these decisions to the provision in Section 812(c) that "where a deduction was allowed of any mortgage or other lien in determining the * * * estate tax of the prior decedent, which was paid in whole or in part prior to the decedent's death, then the deduction allowable under this subsection shall be reduced by the amount so paid." The obvious reference is that if the lien had not been allowed as a deduction in determining the estate tax of the prior decedent, or, if it had not been paid before the present decedent's death, then the property previously taxed should not be reduced by the amount of such lien. Certainly if the purpose of this deduction for property previously taxed is to prevent double taxation on the same property there must be some distinction between the situation where property was taxed in full in the prior decedent's estate and the situation where it was taxed only on a net value after deduction of a mortgage and lien. In the

latter case, since the initial evaluation of property previously taxed is the gross or gross estate valuation, it was necessary that Section 812(c) contain a provision to reduce that evaluation by the previously allowed mortgage or lien deduction. But where the lien did not reduce the valuation which was taxed in the previous estate, the situation is the same as though no lien had existed. The *Thomas v. Earnest* decision specifically modified the *Bahr* decision in recognition of this distinction.

A view contrary to the *Central Hanover* and *Bloedorn* cases was expressed in the case of *Commissioner v. Garland,* CA-1 (1943), 136 F. (2d) 82. In that case the Court explained that "it was contended by the Commissioner before the Board, and again before us, that in determining the present decedent's net estate the deduction allowable under Sec. 303(a)(2) on account of property previously taxed is limited to the value of the present decedent's interest in the estate of the prior decedent at the time of the latter's death, which is to be computed by deducting the debts and obligations of the prior decedent's estate from its gross value". The Court refused to go along with this contention saying that "in effect what the Commissioner asks us to do is to go beyond the permissible limits of statutory interpretation * * *." The Tax Court agreed with this view in the case of *Churchill,* 1944 Tax Court Memo decision Docket 109586 dated March 23, 1944.

The difficulty with the *Bloedorn* and *Central Hanover* line of cases is that the Courts seemed to shy away from the statute to prevent what they thought

might lead to a larger deduction than should be allowed to accomplish the purpose of the statute. They overlooked the fact that the reduction adjustments provided for in the fourth paragraph of Section 812(c) have the effect of correcting what might seem to be an excessive deduction, and adequately prevent any excessive or duplicate deductions. In trying to short-cut the formula prescribed by the statute both the Government and some Courts have reached results which would not have been the answer had the statute been strictly applied according to its terms.

By its very nature a statute such as this cannot produce a perfect result in all situations but it is so composed that it generally produces fair results. An example of what appears to be an unfair result to the taxpayer is a case where certain liens were paid prior to decedent's death, and a strict application of the statute produced what appeared to be a too-low deduction for property previously taxed because of a change in the value of the asset subject to the lien, and in discussing this point the Tax Court said, in the case of *Est. of Lizzie Ransbottom,* 3 TC 1041 (1944):

> "In this proceeding, the decedent received the specific shares of the Ransbottom Brothers Investment Co. common stock, the Charminel Hotel Co. common stock, and the First National Bank stock which were taxed to the prior decedent's estate. These shares, however, were subject to a lien of $29,089.67, and the executors of the estate of the prior decedent took a deduction in this amount on the estate tax return under Schedule L, entitled 'Mortgages and Liens.' These liens were paid in full prior to the decedent's

death. Under these circumstances, the unambiguous language of section 812(c) requires that the 'deduction allowable', which the parties agree is in the amount of $105,173.75, must be reduced by the $29,089.67, which was allowed to the estate of the prior decedent as a deduction for liens. We are not unmindful of the fact that the value of the collateral was substantially less than the amount of the indebtedness and that if such indebtedness was not secured, petitioners would have been entitled to use the amount of $105,-173.75 in computing the net allowable deductions. However, since the wording of the statute is clear and unambiguous, we are not at liberty to enlarge by judicial construction a provision restricting the amount of a deduction. In this situation, we must apply the statute as it is written."

This decision was approved by the Court of Appeals, 6th Circ. 1945—148 F. (2d) 280.

In this case now before this Court a strict application of the statute will produce a fair result. There is no justification for the use of an arbitrary *theoretical* method of computing a deduction allowable under a statute which contains exact rules and formulae for making such a computation. The statute should be followed as it is written.

It is respectfully submitted that Section 812(c) is a clearly defined pattern which will bring forth a product as to which there can be no question. The statute is clear and unambiguous—there can be no doubt of the literal meaning of the requirement that the identifiable value of property previously taxed is

the value used in determining the *gross estate* of the prior decedent and the *gross estate* of the present decedent. Any *theorizing* which ends up in reducing this gross estate value of such property by taxes or indebtedness against the prior estate is a rewriting of the statute which is beyond the province of the Court.

CONCLUSION.

It is respectfully submitted that the District Court erred in concluding that in computing the identified value for property previously taxed, the gross estate valuation of the property previously taxed must be reduced by Federal estate tax and other charges against the first decedent's estate before applying the mathematical computation for adjustment reductions, and the decision of the District Court should be reversed.

Dated, San Francisco, California,
January 11, 1956.

Respectfully submitted,
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(Appendix A Follows.)

Appendix "A"

Appendix A

STATUTES INVOLVED—INTERNAL REVENUE CODE OF 1939.

Sec. 810—RATE OF TAX. A tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 812) shall be imposed upon the transfer of the net estate of every decedent, citizen or resident of the United States, dying after the date of the enactment of this title.

Sec. 811—GROSS ESTATE. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

(a) *Decedent's Interest.*—To the extent of the interest therein of the decedent at the time of his death;

(e) *Joint Interests.*—To the extent of the interest therein held as joint tenants by the decedent and any other person, or as tenants by the entirety by the decedent and spouse, or deposited, with any person carrying on the banking business, in their joint names and payable to either or the survivor, except such part thereof as may be shown to have originally belonged to such other person and never to have been received or acquired by the latter from the decedent for less than an adequate and full consideration in money or money's worth: Provided,

That where such property or any part thereof, or part of the consideration with which such property was acquired, is shown to have been at any time acquired by such other person from the decedent for less than an adequate and full consideration in money or money's worth, there shall be excepted, only such part of the value of such property as is proportionate to the consideration furnished by such other person; *Provided further,* That where any property has been acquired by gift, bequest, devise, or inheritance, as a tenancy by the entirety by the decedent and spouse, then to the extent of one-half of the value thereof, or, where so acquired by the decedent and any other person as joint tenants and their interests are not otherwise specified or fixed by law, then to the extent of the value of a fractional part to be determined by dividing the value of the property by the number of joint tenants.

Sec. 812. NET ESTATE. For the purpose of the tax the value of the net estate shall be determined, in the case of a citizen or resident of the United States by deducting from the value of the gross estate—

(a) *Exemption.*—An exemption of $100,000;

(b) *Expenses, Losses, Indebtedness, and Taxes.*—Such amounts—

(1) for funeral expenses

(2) for administration expenses,

(3) for claims against the estate, and

(4) for unpaid mortgages upon, or any indebtedness in respect to, property where the value of decedent's interest therein, undiminished by such mortgage or indebtedness, is included in the value of the gross estate.

(c) *Property Previously Taxed.*—An amount equal to the value of any property (1) forming a part of the gross estate situated in the United States of any person who died within five years prior to the death of the decedent, or (2) transferred to the decedent by gift within five years prior to his death, where such property can be identified as having been received by the decedent from the donor by gift, or from such prior decedent by gift, bequest, devise, or inheritance, or which can be identified as having been acquired in exchange for property so received. Property includible in the gross estate of the prior decedent under section 811(f) and property included in total gifts of the donor under section 1000(c) received by the decedent described in this subsection shall, for the purposes of this subsection, be considered a bequest of such prior decedent or gift of such donor. This deduction shall be allowed only where a gift tax imposed under Chapter 4, or under Title III of the Revenue Act of 1932, 47 Stat. 245, or an estate tax imposed under this chapter or any prior Act of Congress, was finally determined and paid by or on behalf of such donor, or the estate of such prior decedent, as the case may be, and only in the amount finally determined as the value of such

That where such property or any part thereof, or part of the consideration with which such property was acquired, is shown to have been at any time acquired by such other person from the decedent for less than an adequate and full consideration in money or money's worth, there shall be excepted, only such part of the value of such property as is proportionate to the consideration furnished by such other person; *Provided further,* That where any property has been acquired by gift, bequest, devise, or inheritance, as a tenancy by the entirety by the decedent and spouse, then to the extent of one-half of the value thereof, or, where so acquired by the decedent and any other person as joint tenants and their interests are not otherwise specified or fixed by law, then to the extent of the value of a fractional part to be determined by dividing the value of the property by the number of joint tenants.

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(1) for funeral expenses

(2) for administration expenses,

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(4) for unpaid mortgages upon, or any indebtedness in respect to, property where the value of decedent's interest therein, undiminished by such mortgage or indebtedness, is included in the value of the gross estate.

(c) *Property Previously Taxed.*—An amount equal to the value of any property (1) forming a part of the gross estate situated in the United States of any person who died within five years prior to the death of the decedent, or (2) transferred to the decedent by gift within five years prior to his death, where such property can be identified as having been received by the decedent from the donor by gift, or from such prior decedent by gift, bequest, devise, or inheritance, or which can be identified as having been acquired in exchange for property so received. Property includible in the gross estate of the prior decedent under section 811(f) and property included in total gifts of the donor under section 1000(c) received by the decedent described in this subsection shall, for the purposes of this subsection, be considered a bequest of such prior decedent or gift of such donor. This deduction shall be allowed only where a gift tax imposed under Chapter 4, or under Title III of the Revenue Act of 1932, 47 Stat. 245, or an estate tax imposed under this chapter or any prior Act of Congress, was finally determined and paid by or on behalf of such donor, or the estate of such prior decedent, as the case may be, and only in the amount finally determined as the value of such

property in determining the value of the gift, or the gross estate of such prior decedent, and only to the extent that the value of such property is included in the decedent's gross estate, and only if in determining the value of the net estate of the prior decedent no deduction was allowable under this subsection, section 861(a)(2), or the corresponding provisions of any prior Act of Congress, in respect of the property or property given in exchange therefor.

The following property shall not, for the purposes of this subsection, be considered as property with respect to which a deduction may be allowed: (A) property received from a prior decedent who died after December 31, 1947, and was at the time of such death the decedent's spouse, (B) property received by gift after the date of the enactment of the Revenue Act of 1948 from a donor who at the time of the gift was the decedent's spouse, and (C) property acquired in exchange for property described in clause (A) or (B).

Where, under the provisions of Section 1000(f), a gift received by the decedent was considered as made one-half by the donor and one-half by the donor's spouse, one-half of the gift shall be considered as received by the decedent for each such spouse.

Where a deduction was allowed of any mortgage or other lien in determining the gift tax, or the estate tax of the prior decedent, which was paid in whole or in part prior to the decedent's death, then the deduction allowable under this subsection shall be reduced by the amount so paid. The deduction under this subsection shall be

reduced by an amount which bears the same ratio to the amounts allowed as deductions under subsections (a), (d) and (e) and the amounts of general claims allowed as deductions under subsection (b) as the amount otherwise deductible under this subsection bears to property subject to general claims. If the property includible in the gross estate to which the deduction under this subsection is attributable is not wholly property subject to general claims—

(1) Before the application of the preceding sentence, the amount of the deduction under this subsection shall be reduced by that part of such amount as the value, at the time of the decedent's death, of such property (to which such deduction is attributable) subject to claims but not to general claims is of the value, at the time of the decedent's death, of such property, and

(2) in the application of the preceding sentence in reducing the balance, if any, of such deduction, "the amount otherwise deductible under this subsection" shall be only that part of such amount otherwise deductible (determined without regard to clause (1) of this paragraph) as the value, at the time of the decedent's death, of such property (to which such deduction is attributable) subject to general claims is of the value, at the time of the decedent's death, of such property.

For the purposes of the two preceding sentences and this sentence, "general claims" are the amounts al-

lowed as deductions under subsection (b) which, under the applicable law, in the final adjustment and settlement of the estate may be enforced against any property subject to claims, as defined in subsection (b), and "property subject to general claims" is the value, at the time of the decedent's death, of property subject to claims, as defined in subsection (b), reduced by the value, at the time of the decedent's death, of that part of such property against which amounts allowed as deductions under subsection (b) which are not general claims may be enforced, under the applicable law, in the final adjustment and settlement of the estate. Where the property referred to in this subsection consists of two or more items the aggregate value of such items shall be used for the purpose of computing the deduction.

(d) *Transfers for Public, Charitable, and Religious Uses.*

(e) *Bequests, etc., to Surviving Spouse.*

Sec. 827. LIEN FOR TAX.

(a) *Upon Gross Estate.*—Unless the tax is sooner paid in full, it shall be a lien for ten years upon the gross estate of the decedent, except that such part of the gross estate as is used for the payment of charges against the estate and expenses of its administration, allowed by any court having jurisdiction thereof, shall be divested of such lien. If the Commissioner is satisfied that the tax liability of an estate has been fully discharged or provided for, he may, under regulations prescribed by him with the approval of the

Secretary, issue his certificate, releasing any or all property of such estate from the lien herein imposed.

(b) *Liability of Transferee, Etc.*—If the tax herein imposed is not paid when due, then the spouse, transferee, trustee, surviving tenant, person in possession of the property by reason of the exercise, nonexercise, or release of a power of appointment, or beneficiary, who receives, or has on the date of the decedent's death, property included in the gross estate under section 811(b), (c), (d), (e), (f), or (g), to the extent of the value, at the time of the decedent's death, of such property, shall be personally liable for such tax. Any part of such property sold by such spouse, transferee, trustee, surviving tenant, person in possession of property by reason of the exercise, nonexercise, or release of a power of appointment, or beneficiary, to a bona fide purchaser for an adequate and full consideration in money or money's worth shall be divested of the lien provided in section 827(a) and a like lien shall then attach to all the property of such spouse, transferee, trustee, surviving tenant, person in possession, or beneficiary, except any part sold to a bona fide purchaser for an adequate and full consideration in money or money's worth.